USS For the future

An update on the forthcoming changes to the Universities Superannuation Scheme

Tim Fuery

The changes – a brief summary

KEY FEATURES OF THE SCHEME CHANGES	
DB Section	
Salary link for past service	CPI[1]
DB future benefit design	CRB
DB pension accrual rate	1/75
DB lump sum accrual rate	3/75
DB salary threshold	£55,000
Revaluation of salary threshold	CPI[1]
DB employee contribution rate	8%
Active revaluation of CRB benefits, and indexation	CPI[1]

[1] Assumes 5% and 10% indexation slicing as per current rules on post October 2011 service only.

The changes in summary

KEY FEATURES OF THE SCHEME CHANGES	
DC Section	
Employer DC contributions above threshold	12%
Other employer DC contributions	Up to 1% match on all salary
DC employee contribution rate on salary above the threshold	8%
DC voluntary salary cap	From £55,000
DC investments will be separate from DB and there will be a number of options including a default fund – the options will not be published until early summer	
Employers' contribution commitment	18%
The employer contribution rate will be a uniform 18% of salary for all employers, regardless of the take up by employees of the DC matching contribution arrangement. A minimum employer contribution of 18% will apply for the next two valuations, i.e. up to 31 March 2020.	

[1] Assumes 5% and 10% indexation slicing as per current rules on post October 2011 service only.

The current position

Final salary section and treatment of past service

Pensionable salary at retirement	x	Number of years past service	÷	Accrual rate (1/80th)	=	Pension
£35,000 rising to £45,000 after 10 years	x	10 years	÷	Accrual rate	=	£5, 625 a year

CRB salary section and treatment of past service

Pensionable salary	÷	Accrual rate (1/80th)	=	Pension benefits earned each year		USS pension increases until retirement	=	pension
£35,000	÷	Accrual rate (1/80th)	=	£437 per year	x	Increases of 2.5% for 10 years (437 x 1.025^{10})	=	£559 per year

The new benefit arrangement – new defined benefit section

New defined benefit section for pension benefits provided after the implementation date

- Career revalued benefits

- Improved accrual rate – 1/75th of pensionable salary

- up to a salary threshold, set initially at £55,000, though this threshold will only apply from 1st October 2016. Until that point the CRB section will have no threshold.

Example

Pensionable salary of £35,000 per year	÷	Accrual rate of 1/75ths	=	£466 a year	X	Inflation at 2.5% for 10 years (466 x 1.025^{10})	=	£598 a year
Pensionable salary of £45,000 per year	÷	Accrual rate of 1/75ths	=	£600 a year	X	Inflation at 2.5% for 10 years (600 x 1.025^{10})	=	£768 a year

Pension provision on earnings above the threshold

New defined contribution section from 1st October 2016

-Contributions on pensionable salary above the salary threshold (initially set at £55,000), unless the member sets a voluntary salary cap

- Members' contributions will be 8% and employers contributions will be 12% in respect of salary above the threshold

-Choice of investment options and choice of retirement options

Example – career revalued benefits detail

Pensionable salary of £60,000 per year	X	Accrual rate of 1/75ths applied to first £55,000	=	£733 a year	X	Increases of 2.5% for 10 years ($£733 \times 1.025^{10}$)	=	£916 a year

Employer contribution of 12% of £5,000	+	Member contribution of 8% of £5,000	=	£ 1,000 a year	X	Amount made from investment (5%) for 10 years ($£1000 \times 1.05^{10}$)	=	£1,551 DC account

Employer contribution rate

Current employer contribution rate	Employer contributions for new section
16%	**18%**

The future service benefits to be provided from the implementation date
(that is, the CRB benefits based on the 1/75th formula, plus 3/75ths lump sum, up to a salary threshold, and including death in service and incapacity benefits)

The employer contributions to the funding deficit
(that is the contributions which will be required under the recovery plan to fund the deficit)

The employer contribution to the defined contribution component
(in respect of salaries in excess of the threshold, for relevant members)

The employer contribution to the defined contribution matching facility
(in cases where members choose to make an additional contribution of 1%)

Further Changes – Added years AVC's

- **It will not be possible to enter a new lump sum or regular instalment AVC arrangement after the 30 October 2015.**
- **Regular instalment added years AVC arrangements in place as at 31 March 2016 will continue unless the trustee company is informed otherwise.**
- **The benefits earned from AVC arrangements will be based upon total service secured by the AVC and pensionable salary as at 31 March 2016.**
- **Should you decide to cease your regular instalment AVC arrangement, the service secured will be pro-rated to the date of cessation.**
- **Contributions for regular instalment AVCs, which remain in place after 31 March 2016, will be based upon your actual salary which can differ from pensionable salary.**

Further Changes – Money purchase AVC's

- **If you have a current Prudential money purchase arrangement you will be able to continue making payments after 1st April 2016. However the ability to utilise the fund to buy added years of service at retirement will be restricted to the value of the fund at 31st March 2016 together with any further returns on the fund built up to the 31st March 2016.**
- **Contributions paid in on or after 1st April 2016 would need to be taken as cash at retirement**
- **The primary means of making additional voluntary contributions available after the scheme changes are fully implemented will be the new defined contribution arrangement**
- **You will also be able to transfer the Prudential fund in to another arrangement, if you so choose, as well as being able to take the fund as cash at retirement.**

Further Changes – Transfers In

- **From 1 November 2015 no new non-club transfers-in for members of the final salary section will be accepted.**
- **Requests for a 'club' transfer will be accepted up until two years after the date you join USS.**
- **From 1 April 2016, club transfers-in of previous pension benefits will secure additional pension on a career revalued benefits (CRB) basis.**
- **Once the first phase of the scheme changes has been implemented on 1 April 2016, all active members will be able to transfer-in previous pension benefits to secure additional pension on a career revalued benefits (CRB) non-club basis. This provision will remain in place until the date that the new defined contribution (DC) section is introduced on 1 October 2016, after which transfers-in will only be accepted on a DC basis.**
- **From 1 October 2016, non-club transfers-in will only be accepted into the defined contribution (DC) section.**

USS tax mitigation options - Summary

- **There are further changes to the pensions tax regime from April 2016 including a further reduction in the Life Time Allowance from £1.25m to £1m and the introduction of a tapered annual allowance which will impact specifically on higher earners.**
- **USS currently has a number of tax mitigation options in place but only for members of the Final Salary section.**
- **The existing temporary cessation of accrual options and defer and restart options are being withdrawn**
- **From April 2016 new USS tax mitigation options will be introduced available to all members of USS.**
- **The two options are an Enhanced Opt Out option and a Voluntary Salary Cap option**

LTA changes

- **The LTA limit will change from £1.25m to £1m from April 2016. There will be new protection available such that staff whose LTA is between £1.25m and £1.0m will be able to cease accrual and protect the excess over the £1m from tax. The marginal tax rate applied is 55% and thus the impact is significant.**
- **Staff with more than 30 years service on a salary of £116k, or 35 years on a salary of £100k, or 40 years on a salary of £87k are likely to be affected. Staff who have had a number of pension arrangements over their career should seek information from each provider on the value of their pots to ensure that they are in a position to make an informed decision.**
- **Whether staff should cease accrual is a personal decision and not one which should be taken lightly. Consideration should be given to seeking advice from an IFA if you believe that you are affected.**

AA changes

- **The Annual allowance is remaining at £40k for 2016. However for higher earners the allowance will be tapered.**
- **The taper will apply to those whose adjusted income is greater than £150k where adjusted income equates to salary plus employer pension contributions. For USS members where the employer rate is 18% this means the base income figure would be £127k**
- **For every £2 one exceeds the £150k the annual allowance will be reduced by £1. thus for those with adjusted income of £160k there annual allowance would be £35k.**
- **This will thus impact on only a small number of University staff but will nevertheless impact on people's approach to pension saving.**
- **The highest earning clinicians and academics will find themselves breaching the annual allowance by merely accruing an extra years service regardless of pay awards or increments**

USS tax mitigation options – Enhanced Opt Out

- **The existing Enhanced Opt out option is retained in its current form for the new hybrid scheme with the option being available for all members**
- **The option allows the member to elect to cease accrual of service but maintain death in service and incapacity cover**
- **The option allows members to deal with either LTA or AA threshold problems**
- **The election can be cancelled by the member but must remain in place for at least 12 months**
- **The member is required to contribute 2.5% of salary (or such sum as determined by the trustee) to maintain the cover, and the employer will pay a contribution of 2.1% towards the scheme deficit or such percentage as determined by the scheme actuary**
- **Benefit at retirement is calculated based on service at the election date**
- **Incapacity retirement and death in service benefits are calculated as though the member remained in service and continued to accrue**

USS tax mitigation - Voluntary Salary Cap

- **Members can choose to cap their exposure to the defined contribution scheme by setting a voluntary salary cap at any level over the threshold. The member may choose to do so for a number of reasons including;**
  - **They may exceed the threshold by such a small amount that establishing a DC fund is not advantageous**
  - **They may choose to set a cap as they may otherwise be exposed to an annual allowance charge or a lifetime allowance charge, this will particularly be a risk for higher earners with long service in USS or those who have substantial increases in remuneration.**
- **The cap will be introduced from 1st October 2016 and the election will initially last for 6 months.**
- **Members will be able to choose on an annual basis if they wish to set a voluntary cap but it will apply for the full 12 months of each scheme year i.e. from 1st April to 31st March**
- **The member can choose to maintain full incapacity and death in service cover by paying the appropriate additional contribution**

Employee Engagement

- **USS is changing its approach to member engagement and will in future seek to maximise the use of a new employee portal**
- **The new web portal will be launched on the 4th July 2016 and members will have to register to be able to use the portal**
- **Member choices around participation in the new DC element of the scheme will have to be exercised through the portal and any member wishing to utilise the employer match facility will have to do so through the portal**
- **Members wishing to make investment choices relating to the DC option will also need to do so through the portal**
- **The portal will also support members wishing to access detail on AVC arrangements and will carry a range of modellers to support members seeking retirement information**

Questions

- **USS is continuing to build a portfolio of FAQs on its website and this should address many of the routine queries that members may have**
- **Employers are committed to sharing USS communications with members and we will continue to provide updates on the changes at regular intervals**
- **In the meantime are there any specific questions on what has been presented today**